

FEDERAL ENERGY REGULATORY COMMISSION
WASHINGTON, D.C. 20426

In Reply Refer To:
Office of Enforcement
Docket No. FA19-5-000

October XX, 2020

Chevron Pipe Line Company
Attention: Shawn Chhabra
Manager, Regulatory & Compliance
1400 Smith Street (HOU140 38174)
Houston, TX 77002

Dear Mr. Chhabra:

1. The Division of Audits and Accounting (DAA) within the Office of Enforcement (OE) of the Federal Energy Regulatory Commission (Commission) has completed an audit of Chevron Pipe Line Company (CPL). The audit covered the period January 1, 2014 to December 31, 2018.
2. The audit evaluated CPL's compliance with requirements of the: (1) Uniform System of Accounts Prescribed for Oil Pipeline Companies under 18 C.F.R. Part 352; (2) FERC Form No. 6, Annual Report of Oil Pipeline Companies under 18 C.F.R. Part 357; and (3) Preservation of Records for Oil Pipeline Companies under 18 C.F.R. Part 356;. The audit also evaluated CPL's compliance with select provisions of its FERC transportation tariffs. The enclosed audit report contains five findings of noncompliance and 18 recommendations that require CPL to take corrective action.
3. On September 28, 2020, you notified DAA that CPL does not intend to contest the five findings of noncompliance and corresponding recommendations. A copy of your verbatim response is included as an appendix to this report. I hereby approve the audit report.
4. CPL should submit its implementation plan to comply with the recommendations within 30 days of this letter order. CPL should make quarterly submissions to DAA describing the progress made to comply with the recommendations, including the completion date for each corrective action. As directed by the audit report, these submissions should be made no later than 30 days after the end of each calendar quarter, beginning with the first quarter after this audit report is issued, and continuing until all the corrective actions are completed.

5. The Commission delegated the authority to act on this matter to the Director of OE under 18 C.F.R. § 375.311. This letter order constitutes final agency action. CPL may file a request for rehearing of this letter order with the Commission within 30 days of the date of this order under 18 C.F.R. § 385.713.

6. This letter order is without prejudice to the Commission's right to require hereafter any adjustments it may consider proper from additional information that may come to its attention. In addition, any instance of non-compliance not addressed herein or that may occur in the future may also be subject to investigation and appropriate remedies.

7. I appreciate the courtesies extended to the auditors. If you have any questions, please contact Ms. Kristen Fleet, Acting Director and Chief Accountant, Division of Audits and Accounting at (202) 502-8063.

Sincerely,

Larry R. Parkinson
Director
Office of Enforcement

Enclosure



Federal Energy Regulatory Commission
Office of Enforcement
Division of Audits and Accounting

**Audit of Chevron Pipe Line
Company's (CPL) Compliance with:**

- Uniform System of Accounts Prescribed for Oil Pipeline Companies in 18 C.F.R. Part 352;
- FERC Form No. 6, Annual Report of Oil Pipeline Companies in 18 C.F.R. Part 357;
- Preservation of Records for Oil Pipeline Companies in 18 C.F.R. Part 356; and
- Select Tariff Provisions in CPL's FERC Transportation Tariffs.

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I. Executive Summary

A. Overview

The Division of Audits and Accounting (DAA) within the Office of Enforcement of the Federal Energy Regulatory Commission (Commission) has completed an audit of Chevron Pipe Line Company (CPL or the Company). The audit evaluated CPL's compliance with requirements of the (1) Uniform System of Accounts Prescribed for Oil Pipeline Companies under 18 C.F.R. Part 352; (2) FERC Form No. 6, Annual Report of Oil Pipeline Companies under 18 C.F.R. Part 357; and (3) Preservation of Records for Oil Pipeline Companies under 18 C.F.R. Part 356. The audit also evaluated select provisions of CPL's FERC transportation tariffs. The audit covered the period January 1, 2014 to December 31, 2018.

B. Chevron Pipe Line Company

CPL, headquartered in Houston, Texas, is an indirect wholly owned subsidiary of Chevron Corporation, which is an integrated oil company with upstream, midstream, and downstream operations. Chevron Pipeline and Power, a business unit within Chevron Corporation, directs and oversees the midstream operations of Chevron Corporation, including those of CPL. CPL owns and operates both Commission-jurisdictional and non-jurisdictional assets. During the audit period, CPL had joint and equity ownership interests in several other pipeline companies and provided operational and support services to other pipelines and business units within Chevron Corporation.

Following extensive divestitures, CPL owns and operates a network of about 3,000 miles of Commission-jurisdictional and non-jurisdictional pipeline facilities that transport over 1.2 million barrels of crude oil, natural gas, natural gas liquids, refined petroleum products, liquefied petroleum gas, and petrochemicals on a daily basis within the United States. CPL also operates storage capacity of approximately 2.6 million barrels of the foregoing products. CPL provides transportation, gathering, and terminal and storage services to the petroleum and petrochemical industry in the U.S. Gulf of Mexico, as well as California, Colorado, Louisiana, Texas, and Utah. Of CPL's trunk transportation revenues, 99 percent were earned through interstate movements, with less than 1 percent from intrastate movements, during the audit period. CPL used the Commission's index rate methodology for all interstate transportation movements during the audit period, except for a few involving shippers with negotiated rate agreements.

C. Summary of Compliance Findings

Audit staff identified five areas of noncompliance, summarized below. Section IV of this report contains a detailed discussion of the audit findings.

1. *Depreciation Rates and Reserve Balances* – CPL’s accounting and financial reporting for depreciation included several deficiencies affecting depreciation expense and reserve balances and the accuracy of the Annual Cost of Service Based Analysis Schedule on Page 700 (Page 700) of CPL’s FERC Form No. 6 filings. Specifically, CPL:
 - Did not use Commission-approved depreciation rates to determine depreciation expense. Instead, CPL used slightly higher depreciation rates than the depreciation rates last approved by the Commission, resulting in increased depreciation expense and depreciation reserve balances.
 - Incorrectly continued to accrue depreciation expense on five carrier property asset accounts after the underlying asset accounts had been fully depreciated. This resulted in CPL recording \$11.4 million of excess depreciation expense as of December 31, 2018.
 - Maintained two carrier property asset accounts with negative depreciation reserve balances. This resulted in an inflated net book value for these two accounts that exceeded the original cost of the assets by \$8.2 million as of December 31, 2018.
2. *Accounting for Inactive and Idle Property* – CPL improperly accounted for inactive and idle pipeline assets as carrier property rather than noncarrier property. This affected the accuracy of amounts reported in carrier and noncarrier property and depreciation accounts, and resulted in CPL overstating rate base and depreciation expense on Page 700 in its 2018 FERC Form No. 6.
3. *Noncarrier Property Revenues and Expenses* – CPL improperly accounted for revenues and expenses related to noncarrier property in operating expense and revenue accounts. This resulted in CPL misstating net income from noncarrier property each year of the audit period, with reporting errors ranging from \$3.6 million to \$5.7 million. These errors impacted the accuracy of the information reported in the FERC Form No. 6.
4. *Accounting for Legal Settlements and Regulatory Fees* – CPL improperly accounted for legal settlements relating to employment discrimination claims as an operating rather than nonoperating expense. CPL also improperly accounted for regulatory fees paid to a federal agency in the wrong operating expense account. These errors impacted the accuracy of the information reported in the FERC Form No. 6.

5. *Reporting of Interstate Operating Revenues* – CPL omitted reporting some jurisdictional interstate operating revenues on Page 700 of its 2017 FERC Form No. 6.

D. Recommendations

Audit staff's recommendations to remedy this report's findings are listed below. Section IV also contains these detailed recommendations for each finding. CPL will need to implement corrective actions to address each recommendation.

Depreciation Rates and Reserve Balances

1. Create procedures and controls to ensure depreciation rates remain relevant and applicable, and to make timely revisions when property accounts become fully accrued. Also strengthen procedures and controls to ensure that CPL applies Commission-approved rates to depreciate all carrier property assets and ceases accruing depreciation when assets accounts become fully depreciated.
2. Conduct a depreciation study that reflects current economic conditions and includes other factors, including net salvage and interim retirements. Based on this study, determine whether to continue using CPL's current Commission-approved depreciation rates to calculate the depreciation expense pursuant to Part 347, or to timely file a request to change depreciation rates pursuant to General Instruction 1-8.
3. Submit a copy of this depreciation study to the Commission within 30 days of completion. CPL should also make appropriate changes to its existing depreciation rates when proposed revised rates are approved or modified by the Commission.
4. Submit any necessary accounting entries supporting any proposed adjustments within the accrued depreciation accounts to DAA for review within 30 days of the Commission accepting CPL's proposed depreciation rates. Upon approval from DAA, make needed accounting entries within 30 days.
5. Provide worksheet(s) showing the effect and adjustment made to each component on Page 700 of the FERC Form No. 6.
6. Upon receiving DAA staff's review and response to CPL's accounting entries and worksheets, restate and footnote the balances reported in the

FERC Form No. 6 in the current and comparative years of the report, including all schedules affected, to reflect and disclose the revisions made.

Accounting for Inactive and Idle Property

7. Update accounting policies and procedures to ensure that inactive and idled pipeline assets are accounted for as noncarrier property consistent with the Commission's accounting requirements.
8. Reclassify all inactive and idled pipeline assets recorded in Account 30 that will not be used in CPL's future pipeline operations to Account 34, and reclassify the related accrued depreciation from Account 31 to Account 35. Submit accounting entries supporting adjustments within the carrier and noncarrier property accounts to audit staff for review within 30 days of issuance of this audit report. Upon approval from DAA, make accounting entries supporting this adjustment within 30 days.
9. Perform an analysis to determine the full scale of Page 700 impacts, including impacts to Line 1, Operating and Maintenance Expense; Line 2, Depreciation Expense; Lines 5a-5d, Rate Base; and other lines on Page 700, and provide this analysis to DAA staff for further review.
10. Upon receiving DAA staff's review and response, restate and footnote the balances reported in the FERC Form No. 6 in the current and comparative years of the report, including all schedules affected, to reflect and disclose the revisions made.

Noncarrier Property Revenues, Expenses, and Net Income

11. Establish policies and procedures to ensure that revenues, expenses, and net income associated with noncarrier property are accounted for and reported in accordance with the Commission's accounting regulations.
12. Strengthen procedures to ensure personnel responsible for completing and reviewing the FERC Form No. 6 follow the instructions for completing the schedules prior to submission, to eliminate errors.
13. Reclassify revenues and expenses associated with noncarrier property to Account 620 for the current year. Submit a copy of the journal entries to DAA within 30 days of the issuance of this report.
14. Restate and footnote the income statement balances reported in the FERC Form No. 6 in the current and comparative years of the report for Accounts

600, 610, and 620, including all schedules affected, to reflect and disclose revisions made.

Accounting for Legal Settlements and Regulatory Fees

15. Update policies and procedures to ensure employee discrimination claim settlement payments and regulatory fees are accounted for consistent with the Commission's accounting regulations.
16. Record employee discrimination claim settlement payments in Account 660, Miscellaneous Income Charges, and record regulatory fees, such as PHMSA user fees, in Account 590, Other Expenses, prospectively.

Reporting of Interstate Operating Revenues

17. Develop procedures and controls to ensure pipeline systems sold are appropriately removed from the FERC Form No. 6 Page 700.
18. Strengthen processes to ensure employees perform adequate reviews of interstate operating revenues reported on Page 700 data.

E. Compliance and Implementation of Recommendations

Audit staff further recommends that CPL submit to DAA for review:

- Plans for implementing audit staff's recommendations within 30 days of the issuance of this report.
- Quarterly reports describing CPL's progress in completing corrective actions for each recommendation. CPL should submit these nonpublic quarterly reports no later than 30 days after the end of each calendar quarter, beginning with the first quarter after the Commission issues this report, and continuing each quarter until CPL completes all recommended corrective actions.
- Copies of any written policies and procedures developed or updated in response to this report's recommendations; copies of journal entries made to correct accounting errors and deficiencies; and other information supporting the corrective actions taken. CPL should submit these documents for audit staff's review in the first nonpublic quarterly report after it completes them.

II. Background

A. CPL's Pipeline System

At the start of the audit period, CPL owned and operated a network of almost 10,000 miles of jurisdictional and non-jurisdictional pipeline assets. During the audit period, CPL sold several of its pipeline assets, including Delta Gathering and Mesquite Pipeline in 2014; Eugene Island 341 in 2015; Kettleman Los Medanos / West San Joaquin Valley pipeline, TENDS Ethane/Propane Line and eight Gulf of Mexico pipeline systems in 2016; and Eugene Island Pipeline System in 2017. The sale of these pipeline assets, CPL stated, was intended to optimize the Company's performance by divesting assets that no longer had a strategic fit or that could not compete for capital with other investment alternatives.

Since 2018, CPL has owned and operated a system consisting of about 3,000 miles of pipeline. CPL's Commission-jurisdictional pipeline assets include the Empire Terminal; Fourchon (South Timbalier/Timbalier Bay), Fourchon to Empire, West Bay, Breton Sound, and Salt Lake Crude systems; and Cal-Ky Pipeline.¹ CPL uses these pipeline assets for interstate transportation of crude oil to and from origin and destination points across these systems. CPL's non-jurisdictional pipeline assets include Empire Dock (which loads/unloads crude barges), NW Terminal (connecting to a blending facility), Raven Ridge (a CO₂ pipeline joint venture), and the Northam System (an intrastate pipeline). CPL uses these pipeline assets for intrastate transportation of refined petroleum products, liquefied petroleum gas, and chemicals between origin and destination points within state lines.

CPL also operates pipelines on behalf of other companies, including the Southern California Products Line (refined fuels), Bay Area Products Line (refined fuels), Cross Valley Fuel System (San Joaquin crude and natural gas pipelines), Chevron Phillips Chemical Company LLC (a chemicals pipeline joint venture between Chevron Corporation and Phillips 66), and Amberjack Pipeline Company LLC (a joint venture between CPL and Shell Pipeline Company).

¹ In Docket No. OR11-1-000, on January 31, 2011, the Commission granted CPL a temporary waiver of the filing and reporting requirements in sections 6 and 20 of the Interstate Commerce Act (ICA) with respect to CPL's Cal-Ky pipeline, concluding that the physical characteristics and nature of the Cal-Ky pipeline's operations met the established criteria to approve this waiver. The Commission also granted waiver of Parts 341 and 357 of the Commission's regulations, which is the reason CPL does not include amounts for the Cal-Ky pipeline on Page 700 of its FERC Form No. 6 filings. *See Chevron Pipe Line Company*, 134 FERC ¶ 61,073 (2011).

B. CPL's FERC Tariffs and Rates

CPL's rates are based on the Commission's index rate methodology except for a few rates set by negotiated rate agreements. The Commission has adopted the indexing regime to provide a simplified and generally applicable ratemaking methodology for oil pipelines and to create streamlined procedures related to oil pipeline rates.² Indexing allows oil pipelines to change their tariff rates so long as those rates remain at or below applicable ceiling levels, which change every July 1 based upon an index that tracks industry-wide cost changes. When the Commission created indexing, it also added Page 700 to FERC Form No. 6 to provide cost, revenue, and throughput information so that the Commission and the industry can monitor these indexed rates.³ CPL did not have cost-of-service or market-based rates the during audit period.

CPL provides interstate transportation services to shippers of crude oil on its pipeline system pursuant to FERC Rules and Regulations Tariff No. 1166.5.0. The interstate transportation rates associated with these services are specified in tariff rate sheets that are on file with the Commission.⁴ In 2017 and 2018, CPL transported between 2.374 and 2.392 billion barrel-miles and earned annual revenues, respectively, of approximately \$73 and \$77 million. Of those revenues, CPL earned 99 percent from

² See *Revisions to Oil Pipeline Regulations Pursuant to Energy Policy Act of 1992*, Order No. 561, FERC Stats. & Regs. ¶ 30,985 (cross reference 65 FERC ¶ 61,109) (1993), *order on reh'g and clarification*, Order No. 561-A, FERC Stats. & Regs. ¶ 31,000 (cross reference 68 FERC ¶ 61,138) (1994), *aff'd sub nom. Ass'n of Oil Pipe Lines v. FERC*, 83 F.3d 1424 (D.C. Cir. 1996).

³ *Cost-of-Service Reporting and Filing Requirements for Oil Pipelines*, Order No. 571, FERC Stats. & Regs. ¶ 31,006 (cross reference 69 FERC ¶ 61,102) (1994), *order on reh'g and clarification*, Order No. 571-A, FERC Stats. & Regs. ¶ 31,012 (69 FERC ¶ 61,411) (1994), *aff'd sub nom. Ass'n of Oil Pipe Lines v. FERC*, 83 F.3d 1424 (D.C. Cir. 1996); see also *Revisions to and Electronic Filing of the FERC Form No. 6 and Related Uniform Systems of Account*, Order No. 620, FERC Stats. & Regs. ¶ 31,115 (93 FERC ¶ 61,262) (2000), *reh'g denied*, Order No. 620-A, 94 FERC ¶ 61,130 (2001); *Revisions to Page 700 of FERC Form No. 6*, 144 FERC ¶ 61,049, at PP 29-40 (2013), *reh'g denied*, 148 FERC ¶ 61,235 (2014). All jurisdictional pipelines are required to file Page 700, including pipelines exempt from filing the full Form No. 6. 18 C.F.R. § 357.2(a)(2)-(3).

⁴ CPL FERC Tariffs effective during the audit period were: F.E.R.C. Nos. 1147.24.0-1147.25.0; 1152.23.0-1152.24.0; 1153.10.0-1153.11.0; 1155.19.0-1155.20.0; 1157.19.0-1157.20.0; and 1167.12.0-1167.13.0.

interstate transportation and less than 1 percent from intrastate transportation. Besides these revenues, CPL derived revenues from various surcharges, including inventory management fees, gravity bank administration fees, terminal charges, and truck unloading and loading fees.

C. FERC Form No. 6 Reporting

FERC Form No. 6, Annual Report of Oil Pipeline Companies, is an annual reporting requirement under 18 C.F.R. § 357.2. FERC Form No. 6 is designed to collect financial and operational information from oil pipeline companies subject to the Commission's jurisdiction under the Interstate Commerce Act. In Order No. 571, the Commission adopted a new schedule for FERC Form No. 6 – Page 700, Annual Cost of Service Based Analysis Schedule – starting with reporting year 1995.⁵ CPL's Page 700 was prepared by Regulatory Economics Group, LLC (REG) during the audit period. CPL stated that it used and relied upon REG's expertise and supporting work papers to prepare the information that CPL reported on Page 700, including the development of the rate of return on equity. CPL stated that it reviewed Page 700 for accuracy and compliance with Commission requirements prior to its filing.

The FERC Form No. 6 financial statements and supporting pages include both interstate and intrastate amounts *with the exception* of Page 700, which pertains only to jurisdictional interstate amounts. Page 700 requires pipelines to report total annual cost of service (as calculated under the Opinion No. 154-B methodology), operating revenues, and throughput in barrels and barrel-miles for interstate transportation. Page 700 can be used as a preliminary screening tool to gauge the reasonableness of a company's regulated rates by enabling others to determine whether an oil pipeline's costs of service substantially diverge from revenues generated by its rates. A shipper can compare the

⁵ *Cost of Service Requirements and Filing Requirements for Oil Pipelines*, Order No. 571, FERC Stats. & Regs. ¶ 31,006, at 31,175 (cross-referenced at 69 FERC ¶ 61,102), *order on reh'g and clarification*, Order No. 571-A, FERC Stats. & Regs. ¶ 31,012 (1994) (cross-referenced at 69 FERC ¶ 61,411), *aff'd sub nom. Ass'n of Oil Pipe Lines v. FERC*, 83 F.3d 1424 (D.C. Cir. 1996); *see also Revisions to and Electronic Filing of the FERC Form No. 6 and Related Uniform Systems of Accounts*, Order No. 620, FERC Stats. & Regs. ¶ 31,115 (2000) (cross-referenced at 93 FERC ¶ 61,262), *reh'g denied*, Order No. 620-A, 94 FERC ¶ 61,130 (2001); *Revisions to Page 700 of FERC Form No. 6*, Order No. 783, 144 FERC ¶ 61,049 (2013), *reh'g denied*, Order No. 783-A, 148 FERC ¶ 61,235 (2014).

yearly percentage change in the average barrel-mile rate to determine whether a substantial divergence exists to warrant a challenge to an indexed rate.⁶

The Commission also uses the expense and barrel mile data from Page 700 to support its determination of a proposed oil pipeline transportation rate index adjustment for a five-year, forward-looking period. In its most recent review, the Commission used Page 700 data to determine the index adjustment commencing in July 2016 through June 2021.⁷ The basis for the Commission's next Five-Year Review of the Oil Pipeline Index will be its evaluation of the cost increases, on a dollar per barrel-mile basis, from 2014 to 2019, as reflected on Page 700 of the FERC Form No. 6. The new index rate will be used for oil pipeline rates approved and effective from July 1, 2021 through June 30, 2026.

D. Implementation of the 2017 Tax Cuts and Jobs Act

On December 22, 2017, the President signed into law the Tax Cuts and Jobs Act,⁸ which made a number of changes to the federal tax system, including the reduction of the federal corporate income tax rate from a maximum of 35 percent to a flat 21 percent rate, effective January 1, 2018. Because of the reduced federal corporate income tax rate, companies' accumulated deferred income tax balances did not accurately reflect their future income tax liabilities. For oil pipeline companies, the Commission did not take industry-wide action relating to any effects of these tax changes. Rather, the Commission instructed oil pipelines to file their FERC Form No. 6, Page 700 income tax allowance and cost of service information consistent with the Commission's Revised Policy

⁶ Page 700 of the FERC Form No. 6 provides a simplified presentation of an oil pipeline's jurisdictional cost-of-service and revenues. While Page 700 serves as a preliminary screening aid to evaluate pipeline rates, the information alone on this page is not intended to be used to perform a full and complete cost-of-service review. However, the information reported on Page 700 should be consistent with the ratemaking principles embodied in Opinion No. 154-B, which require the reporting of interstate amounts. *See Williams Pipe Line Company*, Opinion No. 154-B, 31 FERC ¶ 61,377, *order denying reh'g in part, modifying Opinion No. 154-B in part, granting clarification, and denying stay*, Opinion No. 154-C, 33 FERC ¶ 61,327 (1985).

⁷ *Five-Year Review of the Oil Pipeline Index*, 153 FERC ¶ 61,312 (2015), *aff'd sub nom. Ass'n of Oil Pipe Lines v. FERC*, 876 F.3d 336 (D.C. Cir. 2017).

⁸ An Act to provide for reconciliation pursuant to titles II and V of the concurrent resolution on the budget for fiscal year 2018, Pub. L. No. 115-97, 131 Stat. 2054 (2017) (Tax Cuts and Jobs Act).

Statement⁹ and the Tax Cuts and Jobs Act. The Commission explained that it will reflect the impact associated with tax changes in its 2020 five-year review of the oil pipeline index adjustment.

CPL, as a wholly owned subsidiary of Chevron Corporation, participates in a tax sharing group; Chevron Corporation files a consolidated federal tax return, which includes CPL's income and that of other subsidiaries. In implementing the Tax Cuts and Jobs Act, CPL revalued its deferred tax liability by applying the reduced federal income tax rate. In the first quarter of 2018, CPL made entries to reduce its deferred tax liability on its balance sheet and to record an equal amount to income.

CPL reflected this in its 2018 FERC Form No. 6, Page 700, filed in April 2019. In light of Opinion No. 511-C,¹⁰ CPL continued to report a tax allowance on Page 700, Line 8, because its earnings were directly distributed to its parent, a tax paying corporation.

⁹ *Inquiry Regarding the Effect of the Tax Cuts and Jobs Act on Commission-Jurisdictional Rates*, 162 FERC ¶ 61,223 (2018) (Revised Policy Statement).

¹⁰ *SFPP, L.P.*, Opinion No. 511-C, 162 FERC ¶ 61,228 (2018), *reh'g denied*, 166 FERC ¶ 61,142, *clarification granted*, 166 FERC ¶ 61,211 (2019).

III. Introduction

A. Objectives

The audit evaluated CPL's compliance with requirements of the (1) Uniform System of Accounts Prescribed for Oil Pipeline Companies under 18 C.F.R. Part 352; (2) FERC Form No. 6, Annual Report of Oil Pipeline Companies under 18 C.F.R. Part 357; and (3) Preservation of Records for Oil Pipeline Companies under 18 C.F.R. Part 356. The audit also evaluated select provisions of CPL's FERC transportation tariffs. The audit covered the period January 1, 2014 to December 31, 2018.

B. Scope and Methodology

Audit staff performed the following actions to facilitate testing and evaluate CPL's compliance with Commission requirements relevant to this audit:

Audit Planning, Processes and Administration

- *Review of Public Information* – Reviewed publicly available materials to understand CPL's corporate structure and subsidiaries, pipeline systems and operations, and affiliate and parent company relationships. Reviewed Commission filings and orders to understand CPL's regulatory actions with the Commission, including its FERC Form No. 6 and 6-Q filings, FERC Rules and Regulations Tariff, FERC tariff rate sheets, accounting filings, and other regulatory information. Reviewed publicly available information from the Department of Transportation's Pipeline and Hazardous Materials Safety Administration (PHMSA), FERC, Chevron, and media outlets.
- *Conferring with Commission Staff* – Conferred with other Commission offices to ensure that audit report findings were written consistent with Commission precedent and policy.
- *Regulatory Standards and Criteria* – Reviewed regulatory requirements and criteria to evaluate CPL's compliance with each audit objective. These

requirements and criteria included Order Nos. 561,¹¹ 767,¹² 780,¹³ and 783;¹⁴ Opinion Nos. 154-B¹⁵ and 511-C;¹⁶ relevant orders involving CPL; regulations within 18 C.F.R. Parts 352, 356, and 357; provisions within CPL's FERC Rules and Regulations Tariff Nos. 1166.5.0 and 1143.0.0 and tariff rate sheets; and instructions to the FERC Form Nos. 6 and 6-Q.

- *Opening and Closing Conferences* – Held an opening conference to explain the audit process, address questions, clarify basic information, and discuss data requests and site visit procedures subsequent to commencing the audit. At the conclusion of audit field work, held a closing conference to discuss draft audit report findings and recommendations, and next steps in the audit process.
- *FERC Data Requests* – Issued formal data requests and emails to obtain information and documentation not publicly available. Data requests served to collect evidence relating to CPL's policies, procedures, accounting and reporting, and other practices that were evaluated for compliance.
- *Conferences Calls* – Held regular teleconferences with CPL to discuss administrative and technical matters. These discussions clarified audit staff's understanding of the Company's policies, procedures, and other information

¹¹ See *Revisions to Oil Pipeline Regulations Pursuant to Energy Policy Act of 1992*, Order No. 561, FERC Stats. & Regs. ¶ 30,985 (1993) (cross-referenced at 65 FERC ¶ 61,109), *order on reh'g and clarification*, Order No. 561-A, FERC Stats. & Regs. ¶ 31,000 (1994) (cross-referenced at 68 FERC ¶ 61,138), *aff'd sub nom. Ass'n of Oil Pipe Lines v. FERC*, 83 F.3d 1424 (D.C. Cir. 1996).

¹² *Revision to Form No. 6*, Order No. 767, 140 FERC ¶ 61,218 (2012).

¹³ *Filing, Indexing and Service Requirements for Oil Pipelines*, Order No. 780, 143 FERC ¶ 61,137 (2013).

¹⁴ *Revisions to Page 700 of FERC Form No. 6*, Order No. 783, 144 FERC ¶ 61,049 (2013), *order on reh'g*, Order No. 783-A, 148 FERC ¶ 61,235 (2014).

¹⁵ *Williams Pipe Line Company*, Opinion No. 154-B, 31 FERC ¶ 61,377, *order denying reh'g in part, modifying Opinion No. 154-B in part, granting clarification, and denying stay*, Opinion No. 154-C, 33 FERC ¶ 61,327 (1985).

¹⁶ *SFPP, L.P.*, Opinion No. 511-C, 162 FERC ¶ 61,228 (2018), *reh'g denied*, 166 FERC ¶ 61,142, *clarification granted*, 166 FERC ¶ 61,211 (2019).

received in data responses and addressed administrative matters relating to data requests, site visits, and audit progression.

- *Site Visit* – Conducted a site visit to CPL’s headquarters in Houston, TX. The visit provided the opportunity to discuss matters in person, perform on-site inspection and analysis, and observe and evaluate underlying procedures, practices, and controls supporting compliance with Commission oil pipeline regulations; the visit enabled audit staff to:
 - Discuss CPL’s corporate structure, departmental functions, and employee responsibilities, and meet with key company officials.
 - Learn about CPL’s pipeline system, daily operations, and transportation of products – in particular, product movement from origin to destination, as well as marketing, contracting, nominating, scheduling, delivery, and invoicing processes, and to review shipper billing invoices.
 - Interview executives, managers, and operational employees about internal policies and procedures, and their daily application.
 - Discuss and observe management and operation of CPL’s corporate regulatory compliance program.
 - Discuss and observe internal accounting and reporting procedures, processes, and controls.
 - Discuss CPL’s treatment of specific accounting matters, including: carrier and noncarrier property; lease agreements; inter/intrastate transportation revenues and pipeline movements; depreciation rates and studies; construction and interest during construction; operating and nonoperating expenses; cost allocations and affiliate transactions; asset purchases and sales; asset retirements and abandonments; and other accounting matters.
 - Examine CPL’s workpapers that supported the cost-of-service schedule reported on Page 700 of the FERC Form No. 6 and held discussions with employees and the CPL consultant that prepared the workpapers.
- *Audit Testing* – Tested CPL’s compliance with the Commission’s accounting and financial reporting requirements, document retention requirements, and select tariff provisions by evaluating, on a sample basis, evidence supporting the amounts reported in the FERC Form No. 6, and the activities and documents supporting the operational requirements of CPL’s FERC tariffs.

Uniform System of Accounts Requirements

- *Accounting Processes, Procedures, and Controls* – Evaluated CPL’s financial accounting processes, procedures, and controls established to achieve compliance with the accounting requirements under 18 C.F.R. Part 352. Interviewed CPL employees responsible for accounting policies, procedures, and practices to determine how these employees ensure that CPL’s decisions align with the Commission’s accounting requirements.
- *Chart of Accounts* – Reviewed CPL’s chart of accounts to understand its structure and whether CPL’s internal system of accounts mapped properly to the Commission’s Uniform System of Accounts.
- *Accounting Systems* – Discussed CPL’s accounting systems to understand CPL’s operations, inputs and outputs, and the interrelationships between modules and feeder systems supporting CPL’s general ledger and subledgers.
- *Significant Accounting Matters* – Tested select balance sheet and income statement accounts to determine the nature of the transactions recorded and whether the accounting was consistent with the Commission’s requirements. Examples of significant accounting matters examined included:
 - *Depreciation Rates and Expense* – Reviewed CPL’s depreciation rates approved and on file with the Commission. Determined whether CPL applied Commission-approved depreciation rates to calculate depreciation expense. Reviewed depreciation accounts for unusual activities and adjustments.
 - *Affiliate Transactions* – Reviewed affiliate transactions to determine whether CPL recorded revenues and costs, for the goods and services it provided or received, in the appropriate account. Examined shared services assigned, allocated, and recorded on CPL’s books for accuracy.
 - *Operating and Nonoperating Expenses* – Examined operating expense accounts to determine whether CPL included nonoperating expenses (e.g., lobbying, donations, entertainment, penalties, and fines) in operating expense accounts. Also, examined whether CPL recorded operating expenses in the appropriate operating expense accounts.
 - *Interstate and Non-Interstate Revenues* – Evaluated CPL’s accuracy in classifying and reporting transportation and non-transportation revenues. This evaluation covered amounts reported in Account 200, Gathering Revenues; Account 210, Trunk Revenues; Account 220, Delivery

Revenues; Account 230, Allowance Oil Revenue; Account 240, Storage and Demurrage Revenue; Account 250, Rental Revenue; and Account 260, Incidental Revenue.

- *Current and Deferred Income Taxes* – Reviewed the adjustments made to deferred tax accounts associated with the Tax Cuts and Jobs Act of 2017 and Commission Order No. 849.¹⁷ Also reviewed whether Commission Opinion No. 511-C¹⁸ affected CPL’s tax allowance reported on Page 700.
- *Carrier and Noncarrier Property* – Reviewed Accounts 30, Carrier Property; 31, Accrued Depreciation – Carrier Property; 34, Noncarrier Property; and 35, Accrued Depreciation, Noncarrier Property. This included reviewing balances, additions, retirements, adjustments, and transfers in these primary accounts and related subaccounts 100 through 187, in addition to tying the activity in Accounts 31 and 35 to Account 540, Depreciation and Amortization.
- *Subsidiary Investment and Equity Method of Accounting* – Identified CPL’s investments in subsidiary companies. Reviewed balances and activities in Account 20, Investments in Affiliated Companies, during the audit period to determine whether CPL properly excluded subsidiary investment activities from its operating income and expense accounts. Reviewed CPL’s memorandum accounts for their initial investments, equity in the undistributed earnings and losses, and proportional share of dividends received.

FERC Form No. 6 Reporting Requirements

- *Reporting Processes, Procedures, and Controls* – Reviewed and evaluated processes, procedures, and controls for complying with Commission financial reporting requirements in 18 C.F.R. § 357.2. Interviewed employees who performed financial reporting and management oversight.
- *FERC Form No. 6 Preparation and Filing* – Examined procedures for preparing, reviewing, and filing CPL’s FERC Form No. 6 filings. Compared the pages referenced in the financial statements to the supporting schedules of

¹⁷ *Interstate and Intrastate Natural Gas Pipelines; Rate Changes Relating to Federal Income Tax Rate*, Order No. 849, 164 FERC ¶ 61,031 (2018), *reh’g denied*, Order No. 849-A, 167 FERC ¶ 61,051 (2019).

¹⁸ *SFPP, L.P.*, Opinion No. 511-C, 162 FERC ¶ 61,228 (2018), *reh’g denied*, 166 FERC ¶ 61,142, *clarification granted*, 166 FERC ¶ 61,211 (2019).

the FERC Form No. 6 for accuracy. Reviewed supporting pages to determine whether CPL completed the pages according to the instructions.

- *Variance Analysis* – Performed variance analyses of balance sheet and income statement accounts reported in the FERC Form No. 6 filings for the audit period. Analyzed anomalies to identify potential accounting and reporting concerns.
- *Notes to Financial Statements* – Reviewed the Notes to Financial Statements to understand significant accounting policies and events, and to identify potential accounting and reporting concerns.
- *Accuracy and Completeness in Reporting* – Sampled FERC Form No. 6 accounts and reviewed supporting documentation to evaluate whether CPL accurately reported activity and balances in the financial statements and supporting schedules. Traced account balances in the FERC Form No. 6 to CPL's general ledger and reviewed individual schedules and related detail pages for consistent and complete reporting under the FERC Form No. 6 instructions. Some of the more significant examples of testing included:
 - *Operating Revenues* – Evaluated Page 301 for interstate transportation revenues and whether those amounts tied to Page 700, Line No. 10.
 - *Noncarrier Income* – Evaluated noncarrier property to determine whether amounts reported on Page 111, Line No. 33 tied to Page 220, and whether amounts reported on Page 114, Line No. 4 tied to Page 335. Reviewed the revenues and expenses for noncarrier property and whether CPL reported the income associated with those properties accurately on Page 335.
 - *Accrued Depreciation* – Evaluated carrier property accrued depreciation reported on Page 11, Line Nos. 29 and 30 for consistency with Pages 216 and 217. Reviewed accrued depreciation reserve balances reported for each asset account to identify over-accrued and under-accrued balances.
 - *Statistics of Operations* – Evaluated statistics of operations data on Pages 600 and 601 and CPL's process for capturing this information using its volumetric measurement system. Discussed how CPL distinguishes interstate and intrastate movements to report throughput in barrels and barrel-miles on Page 700.
 - *Annual Cost of Service Based Analysis Schedule* – Discussed and reviewed CPL's policies and procedures used to prepare the cost-of-service schedule on Page 700 of the FERC Form No. 6. Obtained and reviewed workpapers

prepared by CPL's consultants and met with the consultants to understand their calculations and account input determinations. The consultants explained each schedule that they had prepared, such as the components of rate base and the derivation of the cost rates for return on equity and debt. The consultants also demonstrated how they derived the interstate percentage and applied it to each account input on the cost of service schedule. Audit staff reconciled the account input balances in the workpapers to the amounts reported on Page 700, and to CPL's general ledger and select pages of the FERC Form No. 6.

Record Retention Requirements

- *General Retention Practices* – Reviewed CPL's administration of its record retention program to ascertain compliance with 18 C.F.R. Part 356. Interviewed employees responsible for record retention to understand processes, procedures, and controls for administration and maintenance of records.
- *Transactional Testing and Document Retention* – Requested documents and records to perform compliance testing for each audit scope area, including premature destruction and retention periods.

FERC Tariff Requirements

- *FERC Tariffs and Rates* – Reviewed CPL's FERC tariffs, including its Rules and Regulations Tariff 1166.5.0 (local tariff) and Tariff 1143.0.0. Reviewed tariff rate sheets associated with CPL's index rates under its local tariff to understand its rates and services.
- *Transportation Rate and Billings* – Reviewed CPL's back-office functions for accounting and billing for the transportation of products nominated, scheduled, and delivered for select shippers. Reviewed CPL's billing cycle for consistency with CPL's tariff, including: the initial entry of a transaction; the creation and issuance of tickets; billing and accounting; and recordkeeping. Reviewed customer billings to test whether the rate charged to shippers corresponded to the rate on file with the Commission, and to determine whether products and volumes invoiced to shippers were accurate. Also, audit staff reconciled invoices for transportation services back to the operating revenues reported in CPL's FERC Form No. 6.

IV. Findings and Recommendations

1. Depreciation Rates and Reserve Balances

CPL's accounting and financial reporting for depreciation included several deficiencies affecting depreciation expense and reserve balances and the accuracy of the Annual Cost of Service Based Analysis Schedule on Page 700 of CPL's FERC Form No. 6 filings. Specifically, CPL:

- Did not use Commission-approved depreciation rates to determine depreciation expense. Instead, CPL used slightly higher depreciation rates than the depreciation rates last approved by the Commission, resulting in increased depreciation expense and depreciation reserve balances.
- Incorrectly continued to accrue depreciation expense on five carrier property asset accounts after the underlying asset accounts had been fully depreciated. This resulted in CPL recording \$11.4 million of excess depreciation expense as of December 31, 2018.
- Maintained two carrier property asset accounts with negative depreciation reserve balances. This resulted in an inflated net book value for these two accounts that exceeded the original cost of the assets by \$8.2 million, as of December 31, 2018.

Pertinent Guidance

- 18 C.F.R. Part 347 – Oil Pipeline Depreciation Studies, in section 347.1, states in relevant part:

(d) *Effectiveness of property account depreciation rates.*
(1) The proposed depreciation rates being established in the first instance must be used until they are either accepted or modified by the Commission. Rates in effect at the time of the proposed revision must continue to be used until the proposed revised rates are approved or modified by the Commission.
- 18 C.F.R. Part 352, General Instruction 1-8, Depreciation Accounting – Carrier Property, states in part:

(b)(2) Carriers shall be prepared at any time upon the direction of the Commission to compute and submit revised percentage rate studies. When a carrier believes that any rate

prescribed by the Commission is no longer applicable, it shall submit the rate which it believes should be established supported by full particulars for consideration by the Commission.

- The 1989 letter order approving CPL's depreciation rates states in part:

Chevron Pipe Line Company shall, effective with the accounts for January 1989 and until further order of the Commission or until the associated property accounts become fully accrued, account for depreciation charges by applying to the ledger value of property owned and used in common carrier operations the rates shown in Appendix A.¹⁹

Background

CPL used composite depreciation rates to compute depreciation expense on carrier property assets. Under this method, CPL should apply the Commission-approved composite depreciation rates against the book cost of carrier property included in each property account to derive depreciation expense. The approved composite depreciation rates are based on the weighted average service lives of the property in each asset group and supported by a depreciation study. CPL submitted a depreciation study to the Commission in 1989. The depreciation study reflected the six jurisdictional pipeline systems that CPL owned and operated and other non-jurisdictional assets. This resulted in the Commission issuing a delegated letter order, establishing CPL's approved depreciation rates. According to the order, these rates were to stay in effect unless and until modified by a subsequent Commission order, which has not occurred since 1989.

Audit staff reviewed CPL's depreciation expense calculations to determine whether CPL consistently applied the Commission-approved depreciation rates for each of its pipeline systems. This review determined that CPL did not apply Commission-approved depreciation rates when calculating depreciation expense for its jurisdictional pipeline systems. CPL also used incorrect depreciation rates for several of its non-jurisdictional assets that have Commission-approved depreciation rates. The review also determined that CPL applied depreciation rates and continued to record depreciation expense on assets in certain property accounts after they became fully depreciated, while other asset accounts had inflated book values because of negative accrued depreciation reserve balances. Below is a detailed account of these issues and their impact on accounting and CPL's Annual Cost of Service Based Analysis Schedule.

¹⁹ *Chevron Pipe Line Company*, 48 FERC ¶ 62,184, at 63,190 (1989).

Commission Approved Depreciation Rates

CPL's most recent depreciation rates were approved by the Commission on September 14, 1989.²⁰ Audit staff identified that CPL applied unapproved, and therefore incorrect, depreciation rates in calculating depreciation expense for its New Orleans Pipeline System, which includes the West Bay, Fourchon (South Timbalier, Timbalier Bay), Fourchon to Empire, Breton Sound and Cal-Ky Pipeline systems. Reflected in the table below are the Commission-approved depreciation rates, and the incorrect rates CPL used for its New Orleans Pipeline System, which consisted of only jurisdictional assets:

Account Number	Account Name	Approved Rate	Incorrect Rate Used
102	Right of Way	1.45%	1.44%
103	Line Pipe	1.00%	1.01%
104	Line Pipe Fittings	2.75%	2.76%
105	Pipeline Construction	1.85%	1.84%
106	Buildings	3.35%	3.37%
109	Machine Tools and Machinery	3.65%	3.67%
111	Oil Tanks	0.00	3.72%
113	Communication Systems	2.30%	2.28%
115	Vehicles and Other Work Equipment	1.75%	1.76%
152	Right of Way	2.20%	2.18%
153	Line Pipe	2.05%	2.04%
154	Line Pipe Fittings	2.05%	2.06%
155	Pipeline Construction	2.85%	2.87%
156	Buildings	8.85%	8.86%
159	Machine Tools and Machinery	3.90%	3.88%
160	Other Station Equipment	2.00%	2.01%
161	Oil Tanks	3.70%	3.72%
162	Delivery Facilities	4.30%	4.32%
163	Communication Systems	4.85%	4.84%
164	Office Furniture and Equipment	6.55%	6.56%
165	Vehicles and Other Work Equipment	13.50%	13.49%
183	Communication Systems	7.25%	7.23%

According to 18 C.F.R § 347.1(d), oil pipelines should use depreciation rates approved by the Commission until the Commission approves other rates. As a result of misapplying depreciation rates, CPL overstated depreciation expense and depreciation

²⁰ *Id.*

reserve balances in its FERC Form No. 6 since its rates were approved in 1989. These incorrect amounts also flowed into the depreciation expense component on Line 2, and accumulated depreciation reserve balance included in the rate base component on Line 5 of its Annual Cost of Service Based Analysis Schedule reported on Page 700 of the FERC Form No. 6.

Over Accrued Depreciation Reserve Balances

In reviewing CPL's application of its depreciation rates, audit staff identified that CPL over accrued depreciation reserve balances for five carrier property accounts. The table below shows the affected carrier property accounts and its asset book costs, accumulated depreciation reserves, and net book values as of December 31, 2018:

Account Number	Account Name	Asset Book Cost (dollars)	Depreciation Reserve (dollars)	Net Book Value (dollars)
115	Vehicles and Other Equipment ²¹	0	2,192,583	(2,192,583)
152	Right of Way	2,174,972	2,913,279	(738,307)
153	Line Pipe	14,003,856	22,248,225	(8,244,369)
159	Machine Tools and Machinery	288,977	384,304	(95,327)
162	Delivery Facilities	19,577,501	19,707,884	(130,383)
	Total Balances	36,045,306	44,446,275	(11,400,969)

Audit staff determined that CPL erred by not ceasing the accrual of depreciation at the time it expensed the entire book cost (less net salvage) of the assets in each carrier property account listed in the table above. In its order approving CPL's depreciation rates, the Commission directed CPL that "until further order of the Commission or until the associated property accounts become fully accrued, account for depreciation charges by applying to the ledger value of property owned and used in common carrier operations the rates shown in Appendix A."²² This meant that CPL was to cease accruing depreciation expense once the asset account was fully depreciated.

The Commission's regulations also require that when a carrier believes that any depreciation rate prescribed by the Commission is no longer applicable, it must submit a revised depreciation rate for consideration by the Commission. Because CPL did not

²¹ All vehicles classified in the gathering function were retired in 2017. CPL indicated that no new vehicles or equipment purchased in 2017 and 2018 had a primary use of gathering. The balance remaining in accumulated depreciation relates primarily to a 2005 insurance recovery received for hurricane damages.

²² *Chevron Pipe Line Company*, 48 FERC ¶ 62,184, at 63,190.

timely file with the Commission to adjust its depreciation rates, the assets in the five carrier property accounts became fully depreciated, even though these assets were still operating and providing carrier service. Accordingly, CPL should have realized that its depreciation rates were no longer applicable, prior to the carrier property accounts becoming fully depreciated and should have taken necessary action to submit revised rates to the Commission based on a new depreciation study.

Negative Depreciation Reserve Balances

Audit staff identified negative (i.e., debit) accrued depreciation reserve balances in two carrier property accounts caused by losses recognized on the sale or retirement of carrier property. For Account 163, CPL reduced the depreciation reserve balance by \$5.9 million when it prematurely retired system control and data acquisition (SCADA) assets due to technical obsolescence in 2008. For Account 166, CPL reduced the depreciation reserve balance by \$3.4 million for the unrecognized loss on the sale of its East and West Bay System in 2012. Collectively, these entries reduced the accrued depreciation reserve balances, thereby, increasing the net book value in Accounts 163 and 166 above book cost. The table below shows the affected carrier accounts and their asset book costs, accrued depreciation reserves, and net book values as of December 31, 2018.

Account Number	Account Name	Asset Book Cost (dollars)	Depreciation Reserve (dollars)	Net Book Value (dollars)
163	Communication Systems	2,348,835	(4,699,806)	7,048,641
166	Other Property	4,772,200	(3,636,540)	8,408,740
	Total Balances	7,121,035	(8,336,346)	15,457,381

Conclusion

Audit staff believes CPL's 1989 depreciation rates are no longer relevant given the age of the study used to develop the depreciation rates, reserve balance anomalies, and the change in economic conditions since that time. To account for changes associated with any component of a depreciation rate, periodic studies should be performed to determine whether existing depreciation rates remain relevant or need to be revised prospectively over the carrier property's remaining service life. While the oil pipeline industry has no date-specific standards for the frequency of performing depreciation studies, Commission regulations do require oil pipeline carriers to keep depreciation rates current. General Instruction 1-8(b)(2) directs pipelines to "be prepared at any time upon the direction of the Commission to compute and submit revised percentage rate studies." Accordingly, CPL should conduct a depreciation study that reflects current economic conditions and addresses the concerns discussed above. Performing regular studies ensures that underlying assumptions and other factors used to determine the useful lives associated with depreciation rates do not become outdated.

Recommendations

DAA recommends that CPL:

1. Create procedures and controls to ensure depreciation rates remain relevant and applicable, and to make timely revisions when property accounts become fully accrued. Also strengthen procedures and controls to ensure that CPL applies Commission-approved rates to depreciate all carrier property assets and ceases accruing depreciation when asset accounts become fully depreciated.
2. Conduct a depreciation study that reflects current economic conditions and includes other factors, including net salvage and interim retirements. Based on this study, determine whether to continue using CPL's current Commission-approved depreciation rates to calculate the depreciation expense pursuant to Part 347, or to timely file a request to change depreciation rates pursuant to General Instruction 1-8.
3. Submit a copy of this depreciation study to the Commission within 30 days of completion. CPL should also make appropriate changes to its existing depreciation rates when proposed revised rates are approved or modified by the Commission.
4. Submit any necessary accounting entries supporting any proposed adjustments within the accrued depreciation accounts to DAA for review within 30 days of the Commission accepting CPL's proposed depreciation rates. Upon approval from DAA, make needed accounting entries supporting this adjustment within 30 days.
5. Provide worksheet(s) showing the effect and adjustment made to each component on Page 700 of the FERC Form No. 6.
6. Upon receiving DAA staff's review and response to CPL's accounting entries and worksheets, restate and footnote the balances reported in the FERC Form No. 6 in the current and comparative years of the report, including all schedules affected, to reflect and disclose the revisions made.

2. Accounting for Inactive and Idle Property

CPL improperly accounted for inactive and idle pipeline assets as carrier property rather than noncarrier property. This affected the accuracy of amounts reported in carrier and noncarrier property and depreciation accounts, and resulted in CPL overstating rate base and depreciation expense on Page 700 in its 2018 FERC Form No. 6.

Pertinent Guidance

- 18 C.F.R. Part 352, General Instruction 1-9, Depreciation Accounting – Noncarrier Property, states:

1-9 Depreciation Accounting – Noncarrier property.

Monthly depreciation charges for all depreciable property recorded in account 34, Noncarrier Property, shall be made to account 620, Income from Noncarrier Property, with concurrent credits to account 35, Accrued Depreciation—Noncarrier Property. The depreciation charges shall be such as to distribute the service values equitably over the service life of the property.

- 18 C.F.R. Part 352, Account 30, Carrier Property, states:

This account shall include the cost of tangible property used in carrier service, or held for such use within a reasonable time under a definite plan for pipeline operations. Separate primary accounts are prescribed for each class of carrier property.

- 18 C.F.R. Part 352, Account 31, Accrued Depreciation – Carrier Property, states:

This account shall be credited with amounts charged to operating expenses or other accounts representing the loss in service value of depreciable carrier property. The service value of depreciable property retired shall be charged to this account. It shall also include other entries as may be authorized by the Commission. Detail of this account shall be maintained by primary property accounts. Separate subsidiary records shall be maintained for the amount of accrued cost of removal other than legal obligations for the retirement of property recorded in account 31, Accrued depreciation—Carrier property.

- 18 C.F.R. Part 352, Account 34, Noncarrier Property, states in part:

This account shall include the cost of tangible property not used in carrier pipeline operations.

- 18 C.F.R. Part 352, Account 35, Accrued Depreciation–Noncarrier Property, states:

This account shall be credited with amounts charged to income, representing the loss in service value of depreciable noncarrier property.

- 18 C.F.R. Part 352, Account 540, Depreciation and Amortization, states:

This account shall include charges for the depreciation and amortization of transportation property. Charges for the amortization of fixed term intangibles relating to common carrier operations shall also be included herein.

- 18 C.F.R. Part 352, Account 620, Income (Net) from Noncarrier Property, states:

(a) This account shall include all noncarrier revenues and expenses from property carried in account 34, Noncarrier Property.

(b) All expenses related to noncarrier property, such as operation and maintenance expenses, depreciation, taxes (except Federal income taxes) and similar expenses, are includible herein.

Background

Carrier property represents assets used to provide interstate and intrastate transportation of crude oil and other by-products. This includes property that is inactive or not in current use but held for future use within a reasonable time under a definite plan for pipeline operations. Property or assets that are not used in pipeline operations or held for future use with a definite plan are noncarrier property. Property or assets classified as noncarrier are considered non-transportation and excluded from Page 700.

Audit staff examined CPL's fixed asset subledger, accounting and reporting, and property records for proper classification of carrier and noncarrier property. Audit staff determined that CPL incorrectly recorded certain inactive and idled pipeline property associated with jurisdictional and non-jurisdictional pipeline systems as carrier rather

than noncarrier property. The table below identifies these inactive and idled pipeline systems, along with the book cost, accrued depreciation, and net book value of each system as of December 31, 2018:

Pipeline System Name	Book Cost (dollars)	Accrued Depreciation (dollars)	Net Book Value (dollars)
Jurisdictional ²³			
Fourchon Systems (Timbalier, S Timbalier)	19,157,970	5,171,983	13,985,987
West Bay System	479,489	137,548	341,941
Salt Lake System ²⁴	TBD	TBD	TBD
Non-Jurisdictional			
CUSA-Wilmington Torrance System	56,809	260,794	(203,985)
Inglewood System	93,682	199,850	(106,168)
Northam System	430,109	1,198,632	(768,523)
Grand Total	20,218,059	6,968,808	13,249,251

CPL recorded the book cost of the inactive and idled pipeline systems in Account 30, Carrier Property, and accumulated depreciation in Account 31, Accrued Depreciation – Carrier Property. According to Account 30 instructions, this account includes “the cost of tangible property used in carrier service or held for such use within a reasonable time under a definite plan for pipeline operations.” Account 31, Accrued Depreciation – Carrier Property, is used to record “amounts charged to operating expenses or other accounts representing the loss in service value of depreciable carrier property.”

Since these pipeline systems were inactive and idle and not held for future carrier service under a definite plan, CPL should have transferred the book cost of these assets to

²³ Besides these jurisdictional pipeline systems, CPL had two other systems with idle and inactive assets – the KLM Pipeline System and the Main Pass System, that were retired in 2018. At the time of retirement, CPL removed the two systems’ combined original costs of \$18,498,791 from carrier property; their net book value was \$4,640,758.

²⁴ Regarding valuation of idle assets on its Salt Lake System, CPL did not provide the cost data that audit staff needed to do the analysis. CPL maintains that, unless there is what CPL refers to as an identifiable segment of a system within CPL’s SAP records, CPL does not maintain cost data for the smaller subsets of idled assets in the general ledger as there is no distinction in CPL’s general ledger between “Active” versus “Idle” status. To identify the individual idle/inactive assets within the fixed asset subledger would require CPL field personnel to go through the subledger and identify idle/inactive assets, similar to when assets are retired after replacement of property units. The recommendations accompanying this finding require CPL to provide the cost data for the Salt Lake System necessary to determine whether and how idle assets are valued.

Account 34, Noncarrier Property, and the associated accrued depreciation to Account 35, Accrued Depreciation – Noncarrier Property. CPL was also required to retire any carrier property that was no longer operational or commercially viable and for which there was no intent or plan to reactivate in the future to Account 31. Further, CPL should have also recorded depreciation expense for the inactive and idle assets properly recorded in Account 34 to Account 620, Income from Noncarrier Property, rather than in Account 540, Depreciation and Amortization Expense. In preparing Page 700, CPL queried the input balances for property that had an “active operating status.” In doing so, CPL incorrectly captured inactive and idled property to complete Page 700, resulting in an overstatement of \$13,249,251 in rate base (Line 5) and about \$400,000 in depreciation expense (Line 2) on Page 700 of CPL’s 2018 FERC Form No. 6.

Recommendations

DAA recommends that CPL:

7. Update accounting policies and procedures to ensure that inactive and idled pipeline assets are accounted for as noncarrier property consistent with the Commission’s accounting requirements.
8. Reclassify all inactive and idled pipeline assets recorded in Account 30 that will not be used in CPL’s future pipeline operations to Account 34, and reclassify the related accrued depreciation from Account 31 to Account 35. Submit accounting entries supporting adjustments within the carrier and noncarrier property accounts to audit staff for review within 30 days of issuance of this audit report. Upon approval from DAA, make accounting entries supporting this adjustment within 30 days.
9. Perform an analysis to determine the full scale of Page 700 impacts, including impacts to Line 1, Operating and Maintenance Expense; Line 2, Depreciation Expense; Lines 5a-5d, Rate Base; and other lines on Page 700, and provide this analysis to DAA staff for further review.
10. Upon receiving DAA staff’s review and response, restate and footnote the balances reported in the FERC Form No. 6 in the current and comparative years of the report, including all schedules affected, to reflect and disclose the revisions made.

3. Noncarrier Property Revenues, Expenses, and Net Income

CPL improperly accounted for revenues and expenses related to noncarrier property in operating expense and revenue accounts. This resulted in CPL misstating net income from noncarrier property each year of the audit period, with reporting errors ranging from \$3.6 million to \$5.7 million. These errors impacted the accuracy of the information reported in the FERC Form No. 6.

Pertinent Guidance

- 18 C.F.R. Part 352, Account 600, Operating Revenues, states:

This account shall include the total revenues included in the operating revenue accounts for the calendar year.
- 18 C.F.R. Part 352, Account 610, Operating Expenses, states:

This account shall include the total expenses included in the operating expense accounts for the calendar year.
- 18 C.F.R. Part 352, Account 620, Income (net) from Noncarrier Property, states:

(a) This account shall include all noncarrier revenues and expenses from property carried in account 34, Noncarrier Property.

(b) All expenses related to noncarrier property, such as operation and maintenance expenses, depreciation, taxes (except) Federal income taxes) and similar expenses, are includible herein.
- FERC Form No. 6, Instruction on Page 220, Noncarrier Property, states in part:

4.) Summarize the revenues and expenses of operated noncarrier properties on schedule 335.
- FERC Form No. 6, Instruction on Page 335, Income from Noncarrier Property, states in part:

1.) State the revenues, expenses, and net income of the respondents during the year from each class of noncarrier property provided for in Account No. 620, Income from Noncarrier Property, in the U.S. of A.

Background

The Commission requires oil pipelines to account for revenues and expenses for carrier and noncarrier property in different accounts. For carrier property, revenues are recorded in Account 600, Operating Revenues, and expenses are recorded in Account 610, Operating Expenses.²⁵ Noncarrier property revenues and expense are recorded on a net basis in Account 620, Income (Net) from Noncarrier Property. Audit staff's review identified inconsistencies in CPL's accounting and reporting for revenues and expenses associated with noncarrier property in Account 34, Noncarrier Property.

For example, CPL reported a \$33.1 million balance in Account 34 as of December 31, 2017. CPL reported the same amount in the Noncarrier Property schedule on Page 220 of the FERC Form No. 6 in that year. Schedule 220 requires oil pipelines to report the book cost of their noncarrier property on this schedule and directs them to report all revenues and expenses on Page 335, Income from Noncarrier Property, in the FERC Form No. 6. On Page 335, CPL reported no revenue and \$4.8 million in expenses for a net loss of \$4.8 million associated with noncarrier property in Account 620, Income (Net) from Noncarrier Property. Based on this review, audit staff identified the following two issues related to CPL's accounting for and reporting on noncarrier property.

Accounting for Noncarrier Property Revenues and Expenses

CPL improperly accounted for revenues and expenses related to noncarrier property in Account 600 and Account 610. Audit staff found that CPL accounted for \$6.9 million of noncarrier revenue in Account 600 and \$6.0 million of noncarrier expenses in Account 610. CPL should have accounted for all the revenues and expenses related to noncarrier property in Account 620. As a result of these errors, CPL's net ending balance in Account 620 was understated by \$5.7 million in 2017, by CPL reporting a net loss of \$4.8 million, instead of net income of \$0.9 million.

Reporting Noncarrier Property Revenues and Expenses

As stated above, CPL reported only \$4.8 million of expenses and no revenue on Page 335 to derive the net loss for Account 620 for 2017. FERC Form No. 6 Page 220 instructs oil pipelines to report the revenues and expenses related to noncarrier property on Page 335 of its FERC Form No. 6. As a result of the accounting misclassification discussed above, CPL did not properly complete Page 335. CPL should have reported the net balance of all revenues and expenses associated with all noncarrier property,

²⁵ Account 600 serves as the primary account for sub-accounts 200-260 and Account 610 serves as the primary account for the 300 and 500 series of accounts.

which was \$6.9 million in revenues and \$6.0 million in expenses, to derive net income on noncarrier property of \$0.9 million.

While the discussion focused on 2017, audit staff notes that these deficiencies occurred throughout the audit period. The table below shows the impact on Income from Noncarrier Property (Page 335) for each year of the audit period.²⁶

Year	Revenues (dollars)	Expenses (dollars)	Correct Income (dollars)	As Reported Income (dollars)	Reporting Error (dollars)
2014	6,027,950	1,648,044	4,379,906	(1,187,714)	5,567,620
2015	7,085,663	2,422,232	4,663,431	(569,746)	5,233,177
2016	5,365,838	4,445,951	919,887	(2,663,359)	3,583,246
2017	6,997,856	6,087,953	909,903	(4,793,869)	5,703,772
2018	6,074,330	(5,453,777) ²⁷	11,528,107	6,916,981	4,611,126

Audit staff found that CPL used data from cost centers classified as jurisdictional carrier (active) property to prepare Page 700. As a result, these deficiencies did not affect Page 700 as the revenues and expenses associated with all noncarrier property were captured in cost centers associated with noncarrier (inactive) property. Nonetheless, appropriate accounting and reporting of noncarrier revenue, expenses, and net income will increase transparency to users of the FERC Form No. 6.

Recommendations

We recommend that CPL:

11. Establish policies and procedures to ensure that revenues, expenses, and net income associated with noncarrier property are accounted for and reported in accordance with the Commission's accounting regulations.
12. Strengthen procedures to ensure personnel responsible for completing and reviewing the FERC Form No. 6 follow the instructions for completing the schedules prior to submission, to eliminate errors.

²⁶ As discussed in Finding 2, CPL incorrectly classified inactive and idled pipeline systems as carrier, rather than noncarrier, property in 2018. The table does not reflect the operating results for these systems, since they were incorrectly classified as carrier property in 2018. For that year, these systems did not have any revenue, but continued to be depreciated. As a result, these systems would have decreased noncarrier income.

²⁷ Noncarrier Expenses in 2018 included an ARO Depreciation expense reversal adjustment of (\$7,344,899).

13. Reclassify revenues and expenses associated with noncarrier property to Account 620 for the current year. Submit a copy of the journal entries to DAA within 30 days of the issuance of this report.
14. Restate and footnote the income statement balances reported in the FERC Form No. 6 in the current and comparative years of the report for Accounts 600, 610, and 620, including all schedules affected, to reflect and disclose revisions made.

4. Accounting for Legal Settlements and Regulatory Fees

CPL improperly accounted for legal settlements relating to employment discrimination claims as an operating rather than nonoperating expense. CPL also improperly accounted for regulatory fees paid to a federal agency in the wrong operating expense account. These errors impacted the accuracy of the information reported in the FERC Form No. 6.

Pertinent Guidance

- 18 C.F.R. Part 352, Account 390, Other Expenses, states:

This account shall include the expenses of aircraft, vehicles, and work equipment used in support of operations and maintenance activities; travel, lodging, meals, memberships, and other expenses of operating and maintenance employees; and other related operating and maintenance expenses that are not defined or classified in other accounts.

- 18 C.F.R. Part 352, Account 580, Pipeline Taxes, states:

(a) This account shall include accruals for taxes of all kinds, excepting income taxes (see definition 30(a)), relating to carrier property, operations, privileges and licenses.

(b) The detail of this account shall show separately the amounts levied by the Federal government and by each state.

- 18 C.F.R. Part 352, Account 660, Miscellaneous Income Charges, states in part:

(a) This account shall include income charges not provided for elsewhere chargeable to income accounts for the current year, such as amortization of debt expense, losses on sale or disposition of land and noncarrier property, losses on sales or reductions in value of investment securities (including increases in the valuation allowance within account 11 for the marketable equity securities included in current assets), bad debts, losses on company bonds reacquired, taxes (other than Federal income taxes) on investment securities, trust management expenses, amortization of intangibles which are not restricted to a fixed term, and the difference between the premium and the added

cash surrender value of life insurance on officers and employees when the carrier is beneficiary.

- 18 C.F.R. Part 352, Account 590, Other Expenses, states:

This account shall include the cost of expenses expended for administrative and general services including, the expenses of aircraft, vehicles, and work equipment used for general purposes; travel, lodging, meals, memberships, and other expenses of general employees and officers; utilities services; and all other incidental general expenses not defined or classified in other accounts.

- Accounting Release (AR) No. 12, Discriminatory Employment Practices, states in part:

Question: What is the proper accounting treatment for expenditures made by the utility, resulting from employment practices that were found to be discriminatory by a judicial or administrative decree or that were the result of a compromise settlement or consent decree?

Answer: The Uniform System of Accounts provides that all charges to utility operating expense accounts must be just and reasonable. Expenditures of the nature mentioned above that can be readily identified and quantified should not be considered as just and reasonable charges to utility operations and should be classified to the appropriate nonoperating expense accounts.²⁸

Background

CPL incurred operating and nonoperating expenses during the audit period. Operating expenses represent necessary costs for pipeline operations and are generally includable in cost of service determinations. On the other hand, nonoperating expenses generally do not benefit customers and are excluded from cost of service determinations. Audit staff examined select transactions to determine whether CPL recorded operating and nonoperating expenses in the appropriate accounts. The review determined that CPL

²⁸ *Accounting Release No. 12, Discriminatory Employment Practices*, effective Feb. 1, 1980, <http://www.ferc.gov/enforcement/acct-matts/docs/ar-12.asp> (unpublished order).

misclassified costs for certain legal settlements related to employment discrimination claims as operating rather than nonoperating expenses. CPL also misclassified regulatory fees paid to a federal agency in an incorrect operating expense account.

Legal Settlements

Audit staff's review identified that CPL improperly accounted for legal settlements involving employment discrimination claims. CPL attributed this accounting oversight to the infrequency of its employees processing and accounting for legal settlement payments. While the amount was relatively minor, the accounting for operating and nonoperating expenses is important for cost of service determinations. In accordance with the requirements of AR No. 12, Discriminatory Employment Practices, expenditures made by CPL resulting from employment practices found to be discriminatory by a judicial or administrative decree or that resulted from a compromise settlement or consent decree must be charged as nonoperating expenses.

CPL should have recorded these legal settlements in Account 660, Miscellaneous Income Charges, a nonoperating expense account that generally is not included in the cost of service determinations. Further, these payments were avoidable and unnecessary to operate CPL's pipeline and provide its customers transportation service. Based on audit staff's review of the accounting entries, the settlements identified did not impact cost centers CPL included in its queries to prepare Line 1, Operating Expenses for Page 700. While audit staff's testing focused on 2017 and 2018 transactions, CPL indicated similar accounting likely occurred in other years of the audit period.

Regulatory Fees

Audit staff's review identified CPL incorrectly accounted for regulatory fees paid to PHMSA. PHMSA assesses such fees to CPL and other pipelines to fund its Pipeline Safety program. CPL recorded these fees in Account 580, Pipeline Taxes, rather than Account 590, Other Expenses. Account 580 was not appropriate, as it is used to record tax expenses other than income taxes, such as property taxes. Account 590, Other Expenses, is appropriate, as the PHMSA regulatory fees involved here are representative of administrative and general expenses not defined in another 500 series account. Since both accounts record operating expenses, CPL's accounting did not impact the cost of service schedule on Page 700. While audit staff performed testing in 2018, CPL indicated similar accounting likely occurred in other years of the audit period.

Recommendations

DAA recommends that CPL:

15. Update policies and procedures to ensure that employee discrimination claim settlement payments and regulatory fees are accounted for consistent with the Commission's accounting regulations.
16. Record employee discrimination claim settlement payments in Account 660, Miscellaneous Income Charges, and record regulatory fees, such as PHMSA user fees, in Account 590, Other Expenses, prospectively.

5. Reporting of Interstate Operating Revenues

CPL omitted reporting some jurisdictional interstate operating revenues on Page 700 of its 2017 FERC Form No. 6.

Pertinent Guidance

- FERC Form No. 6, Instructions, Annual Cost of Service Based Analysis Schedule, Page 700, states in relevant part:²⁹

3.) Enter on line 10, columns (b) and (c), total interstate operating revenue, as reported on page 301, for the current and previous calendar years.

- In Order No. 620-A, the Commission stated:³⁰

The Commission never intended in the Final Rule to have a pipeline report its non-jurisdictional costs on page 700. . . . [W]e take this opportunity to clarify Order No. 620 that the cost-of-service and revenue data reported on page 700 will be the cost of service and revenues related to FERC jurisdictional services.

Background

In Order No. 571, the Commission adopted a new FERC Form No. 6 schedule, Page 700, Annual Cost of Service Based Analysis Schedule, starting with reporting year 1995. This schedule allows a shipper to compare proposed changes in revenues against the change in the level of a pipeline's cost of service. Page 700, Instruction No. 3, requires oil pipelines to enter total interstate operating revenue on line 10, columns (b) and (c). The Commission clarified that cost and revenue information reported on lines (1) through (10) of Page 700 data should include interstate-only data, consistent with the

²⁹ The amounts reported in the FERC Form No. 6 include both interstate and intrastate amounts. However, Page 700 reports only interstate amounts, which represent Commission-jurisdictional amounts.

³⁰ *Revisions to and Electronic Filing of the FERC Form No. 6 and Related Uniform System of Accounts*, Order No. 620-A, *order on reh'g*, 94 FERC ¶ 61,130, at 61,498 (2001).

Commission's regulation of interstate oil pipeline rates and the Commission's intent that Page 700 enable the Commission and shippers to analyze interstate pipeline costs.³¹

Audit staff reviewed the 2017 FERC Form No. 6, Page 700 input account balances, supporting documentation, and calculations to determine whether CPL's workpapers fully supported amounts reported on Page 700.³² To determine the accuracy of the input account balances, audit staff traced amounts from Page 700 workpapers to FERC Form No. 6, Page 301 and back to the general ledger. Audit staff determined that all account input balances agreed with one exception. CPL underreported operating revenues by \$859,317 on Page 700, Line 10; CPL reported \$70,213,160 as interstate operating revenues, but CPL should have reported \$71,072,477.

Given that CPL engaged in both interstate and intrastate activities, CPL generally adjusted operating revenue amounts to ensure that it only reported interstate amounts on Page 700. CPL explained that the one exception found by audit staff was an oversight that occurred because it did not properly factor in the impact of the West Delta 109 pipeline system sold in 2016. Audit staff confirmed that CPL excluded West Delta 109 intrastate revenues from Page 700, prior to selling this system in 2016. CPL made this exclusion based on a fixed percentage of total revenues each year.

CPL explained that a new employee responsible for determining revenues inadvertently applied the fixed percentage, despite the fact CPL no longer owned West Delta 109 and no longer received revenues from it, and backed out \$859,317 from the interstate revenues to be reported in the 2017 FERC Form No. 6, Page 700, Line 10. While this error only affected the Page 700 for 2017, appropriate reporting is important to ensure shippers can compare proposed changes in operating revenues against the change in the level of a pipeline's cost of service on Page 700 each year.

Recommendations

DAA recommends that CPL:

17. Develop procedures and controls to ensure pipeline systems sold are appropriately removed from the FERC Form No. 6, Page 700.
18. Strengthen processes to ensure employees perform adequate reviews of interstate operating revenues reported on Page 700 data.

³¹ *Id.*

³² Page 700 of the FERC Form No. 6 provides a simplified presentation of an oil pipeline's estimated jurisdictional cost-of-service and revenues.

V. Company Response



Shawn Chhabra
Manager, Regulatory and Volumetric Accounting
FERC Chief Compliance Officer

September 28, 2020

Kristen Fleet
Acting Director and Chief Accountant
Division of Audits and Accounting
Office of Enforcement
Federal Energy Regulatory Commission
888 First Street NE, Room 51-59
Washington, DC 20426

**Re: Chevron Pipe Line Company
Response to FERC Audit Findings and Recommendations
FERC Docket No. FA19-5-000**

Dear Ms. Fleet:

Chevron Pipe Line Company ("CPL") appreciates the opportunity to comment on the findings and recommendations outlined in the draft audit report issued by the Division of Audits and Accounting on September 11, 2020 (the "Draft Report").

The Draft Report identifies five (5) findings of noncompliance and eighteen (18) associated recommendations. CPL does not contest the findings. As detailed within, CPL in many instances has already implemented corrective actions associated with recommendations in the Draft Report and is diligently working to finalize remaining items.

CPL appreciates the time and effort that your staff has dedicated to this audit. I would like to thank the FERC audit staff for their professionalism, thoroughness and responsiveness throughout this process. CPL values its strong relationship with the Federal Energy Regulatory Commission, and we look forward to working with you to conclude this matter.

Sincerely,

A handwritten signature in black ink, appearing to read "Shawn Chhabra", written over a horizontal line.

Shawn Chhabra
Manager, Regulatory and Volumetric Accounting
FERC Chief Compliance Officer

Midstream
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Page 2

Finding 1- Depreciation Rates and Reserve Balances:

CPL's accounting and financial reporting for depreciation included several deficiencies affecting depreciation expense and reserve balances and the accuracy of the Annual Cost of Service Based Analysis Schedule on Page 700 of CPL's FERC Form No.6 filings.

...

DAA recommends that CPL:

- 1. Create procedures and controls to ensure depreciation rates remain relevant and applicable, and to make timely revisions when property accounts become fully accrued. Also strengthen procedures and controls to ensure that CPL applies Commission-approved rates to depreciate all carrier property assets and ceases accruing depreciation when asset accounts become fully depreciated.*
- 2. Conduct a depreciation study that reflects current economic conditions and includes other factors, including net salvage and interim retirements. Based on this study, determine whether to continue using CPL's current expense pursuant to Part 347, or to timely file a request to change depreciation rates pursuant to General Instruction 1-8.*
- 3. Submit a copy of this depreciation study to the Commission within 30 days of completion. CPL should also make appropriate changes to its existing depreciation rates when proposed revised rates are approved or modified by the Commission.*
- 4. Submit any necessary accounting entries supporting any proposed adjustments within the accrued depreciation accounts to DAA for review within 30 days of the Commission accepting CPL's proposed depreciation rates. Upon approval from DAA, make needed accounting entries within 30 days.*
- 5. Provide worksheet(s) showing the effect and adjustment made to each component on Page 700 of the FERC Form No. 6.*
- 6. Upon receiving DAA staff's review and response to CPL's accounting entries and worksheets, restate and footnote the balances reported in the FERC Form No. 6 in the current and comparative years of the report, including all schedules affected, to reflect and disclose the revisions made.*

CPL's Response:

CPL accepts this finding. CPL's Finance Team has updated its accounting policies and procedures for fixed asset accounting. CPL has developed and implemented procedures to ensure Commission-approved rates are utilized for carrier property assets, including the calculation of depreciation expense within Page 700. Importantly, CPL filed for new depreciation rates on August 12, 2020 in Docket No. DO20-37-000. Upon approval by the Commission, CPL will review for accuracy all changes to depreciation rates within the property accounting system. CPL will also provide DAA with the above-requested analysis of prospective accounting entries to the new rates and impact of adjusted depreciation rates to each component of the Page 700 of the FERC Form No. 6. The completion date is currently estimated to be January 31, 2021. Furthermore, CPL plans to file 2020 FERC Form No. 6 such that it properly reflects the approved revised rates.

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Finding 2- Accounting for Inactive and Idle Property:

CPL improperly accounted for inactive and idle pipeline assets as carrier property rather than noncarrier property. This affected the accuracy of amounts reported in carrier and noncarrier property and depreciation accounts, and resulted in CPL overstating rate base and depreciation expense on Page 700 in its 2018 FERC Form No. 6.

...

DAA recommends that CPL:

- 7. Update accounting policies and procedures to ensure that inactive and idled pipeline assets are accounted for as noncarrier property consistent with the Commission's accounting requirements.*
- 8. Reclassify all inactive and idled pipeline assets recorded in Account 30 that will not be used in CPL's future pipeline operations to Account 34, and reclassify the related accrued depreciation from Account 31 to Account 35. Submit accounting entries supporting adjustments within the carrier and noncarrier property accounts to audit staff for review within 30 days of issuance of this audit report. Upon approval from DAA, make accounting entries supporting this adjustment within 30 days.*
- 9. Perform an analysis to determine the full scale of Page 700 impacts, including impacts to Line 1, Operating and Maintenance Expense; Line 2, Depreciation Expense; Lines 5a-5d, Rate Base; and other lines on Page 700, and provide this analysis to DAA staff for further review.*
- 10. Upon receiving DAA staff's review and response, restate and footnote the balances reported in the FERC Form No. 6 in the current and comparative years of the report, including all schedules affected, to reflect and disclose the revisions made.*

CPL's Response:

CPL agrees with this finding. Idle pipeline assets were transferred to noncarrier property in November 2019. CPL's Asset Retirement Obligation and Idle Property accounting procedures and policies have been updated to ensure compliance with carrier property requirements. CPL will provide DAA with the above-requested analysis to determine the full scale of the 2018 Page 700 impacts. CPL believes that the impacts are immaterial. The completion date is currently estimated to be January 31, 2021.

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Finding 3- Noncarrier Property Revenues, Expenses, and Net Income:

CPL improperly accounted for revenues and expenses related to noncarrier property in operating expense and revenue accounts. This resulted in CPL misstating net income from noncarrier property each year of the audit period, with reporting errors ranging from \$3.6 million to \$5.7 million. These errors impacted the accuracy of the information reported in the FERC Form No. 6.

...

DAA recommends that CPL:

- 11. Establish policies and procedures to ensure that revenues, expenses, and net income associated with noncarrier property are accounted for and reported in accordance with the Commission's accounting regulations.*
- 12. Strengthen procedures to ensure personnel responsible for completing and reviewing the FERC Form No. 6 follow the instructions for completing the schedules prior to submission, to eliminate errors.*
- 13. Reclassify revenues and expenses associated with noncarrier property to Account 620 for the current year. Submit a copy of the journal entries to DAA within 30 days of the issuance of this report.*
- 14. Restate and footnote the income statement balances reported in FERC Form No. 6 in the current and comparative years of the report for Accounts 600, 610, and 620, including all schedules affected, to reflect and disclose revisions made.*

CPL's Response:

CPL agrees with this finding. Importantly, revenue and expense carrier and non-carrier classifications were accurately stated in the FERC Form No. 6 for 2019. CPL's accounting procedures and policies have been updated to ensure compliance with noncarrier property revenue and expense requirements. As such, CPL believes it has addressed each of the related audit recommendations.

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Finding 4- Accounting for Legal Settlements and Regulatory Fees:

CPL improperly accounted for legal settlements relating to employment discrimination claims as an operating rather than nonoperating expense. CPL also improperly accounted for regulatory fees paid to a federal agency in the wrong operating expense account. These errors impacted the accuracy of the information reported in the FERC Form No. 6.

...

DAA recommends that CPL:

- 15. Update policies and procedures to ensure that employee discrimination claim settlement payments and regulatory fees are accounted for consistent with the Commission's accounting regulations.*
- 16. Record employee discrimination claim settlement payments in Account 660, Miscellaneous Income Charges, and record regulatory fees, such as PHMSA user fees, in Account 590, Other Expenses, prospectively.*

CPL's Response:

CPL agrees with this finding. CPL updated its accounting policies and procedures to ensure accurate mapping for legal settlements related to employment and personal injury claims to FERC Account 660 (Miscellaneous Income/Charges) and regulatory fees to federal agencies to Account 590 (Other Expenses). As such, CPL believes it has addressed each of the related audit recommendations through the update of its policies and procedures.

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Finding 5- Reporting of Interstate Operating Revenues:

CPL omitted reporting some jurisdictional interstate operating revenues on Page 700 of its 2017 FERC Form No. 6.

...

DAA recommends that CPL:

- 17. Develop procedures and controls to ensure pipeline systems sold are appropriately removed from the FERC Form No. 6, Page 700.*
- 18. Strengthen processes to ensure employees perform adequate reviews of interstate operating revenues reported on Page 700 data.*

CPL's Response:

CPL agrees with this finding. The omission of some jurisdictional operating revenues only occurred in 2017. CPL updated its Page 700 Desk Procedures to ensure all FERC jurisdictional transportation revenues are included in the future. As such, CPL believes it has addressed each of the related audit recommendations through the update of its policies and procedures.